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SUBJECT: ROSE COLORED GLASSES??? THE UAE 2009 ECONOMIC OUTLOOK

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Classified by Ambassador Richard Olson for reasons 1.4 (b,d).

11. (U) This is a joint Embassy Abu Dhabi - Consulate General Dubai cable.

12. (C) Summary. What was initially widespread denial that the global downturn would impact the UAE's development plans has now transitioned into open expressions of concern about economic prospects for 2009. Government contacts still argue that the UAE will manage positive GDP growth and that, in the medium-term, the slowdown will be beneficial. However, some private sector contacts are deeply concerned, in part because government efforts have not been sufficiently transparent to allay their fears. While impact on the UAE in 2009 is far from clear, the unique structure of the economy may bring a much-needed respite in inflation along with a calming correction to the high profile project craze of 2004-2008. End Summary.

BOOM YEAR ENDS ON A SOUR NOTE

13. (C) UAE economic news in the closing weeks of 2008 did little to inspire confidence about the new year. Local stock indexes fell to 2004 levels, major firms like Dubai's Nakheel delayed projects and fired some employees, ratings agencies downgraded outlooks for parastatal firms and local banks (including Dubai Electricity and Water Authority (DEWA) and Abu Dhabi Commercial Bank (ADCB)), oil prices fell dramatically, and Abu Dhabi Investment Authority (ADIA) was reported to have been a (minor) victim of the Bernie Madoff investment fraud. Without doubt, ADIA, like all holders of diversified equity portfolios, has seen a significant decline in the value of its holdings. Interbank lending rates continue to exceed four percent, despite government liquidity facilities. All in all, there was little to celebrate in the holiday season, apart from an extended public sector vacation in December and competing "world record" fireworks displays in Abu Dhabi and Dubai.

POSITIVE GOVERNMENT SPIN...

14. (C) Despite these negative developments, government officials continue to project optimism about 2009. In Abu Dhabi, senior officials argue that cheap oil production, ADIA's careful investments and economic diversification will all help ensure 2009 brings necessary consolidation and a welcome breather from what some perceived as overly rapid growth. Federal and local budget expenditures will increase almost 20 percent, providing fiscal stimulus and helping ensure the largest private sector entities will survive. Officials argue that consolidation in many sectors (e.g., real estate, construction and finance) will create leaner and stronger firms. Prime Minister and Ruler of Dubai Sheikh Mohammed bin Rashid Al Maktoum echoed this optimistic line to CODEL Dorgan in mid-December, while complaining about the widespread rumors of

Dubai's imminent demise.

...DOESN'T ALLAY PUBLIC CONCERN

15. (C) Despite the positive official spin, the lack of transparency about how exactly the government is addressing the crisis has led many private sector contacts to fear a painful adjustment in 2009. Announced and expected consolidations mean many firms, including quasi-public entities, will scale back planned expansions and/or be forced to cancel announced projects. The resulting job losses and broader impact on economic growth are of great concern to Emiratis and resident expatriates (who have become quite accustomed to ever-expanding economic opportunity in recent years). In particular, falling oil prices, speculation about ADIA's losses, uncertainty about Dubai's debt burden, and continued stock market instability have significantly dampened the exuberance of a few months ago.

2009 GROWTH LIKELY TO SLOW,
BUT NOT DIP TO RECESSION

16. (C) Predictions for 2009 vary. While many expect the global economy will recover from its current downturn in the first or second quarter, contacts fear the UAE could witness a longer downturn in 2009. As indications of a slowdown did not appear until fall 2008, some fear the UAE may not recover until 2010. However, government officials and private analysts all predict 2009 real GDP growth will be positive, if only between two and three percent.

17. (C) The unusual structure of the UAE economy (and others in the region) helps to minimize the impact of an economic slowdown. Unemployment is largely irrelevant to Emirati nationals, as their jobs are usually protected and expatriate workers simply depart (or are expelled from) the UAE if they lose their jobs. Nationals and

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expatriates who keep their jobs are in fact likely to see an increase in standards of living. As global commodity prices fall, and real estate becomes cheaper, inflation is expected to decline (from an average of almost 10 percent in recent years). A rising U.S. dollar (relative to 2008 lows) means that food and other consumer imports will become cheaper, while worker remittances also increase in value.

Major contractors report that costs, including labor and construction materials, are already falling as demand declines.

18. (C) Comment. The economic slowdown calls into question the fundamental strength of the UAE's "if you build it, they will come" development model. 2009 will reveal if Dubai's enormous ambitions were built on leverage that is no longer possible to secure in today's global economy - or on actual demand for a regional commercial center, financial services, tourism, etc. Dubai is still an island of liberal economies, social tolerance and freehold property rights in a region of over a billion people and burgeoning middle classes. While Abu Dhabi's overall financial strength will guarantee its continued economic development, officials may choose to downsize its ambitions to reflect the new reality of the global financial system. End Comment.

OLSON